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2 February 1968

MEMORANDUM FOR: Director of Central Intelligence

SUBJECT : Pricing the Soviet Military Machine

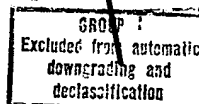
1. At our pre-USIB meeting on 11-8-67, you asked at one point, "Who takes these estimates we make and hangs them all together on the wall to see if the Soviets can afford what we credit them with?" The answer, of course, is, we in CIA do.

2. Specifically, this is a major and continuing responsibility of the Office of Strategic Research. Moreover, this is a unique responsibility of CIA, for the work OSR does on Soviet military economics is not duplicated elsewhere in the Community. This is by agreements reached between Mr. McCone and the Secretary of Defense in 1964. OSD and DIA in particular depend on us for this analysis, and we service requests from them.

3. In addition to giving you a brief explanation of the military-economic process to put in your pocket -- it is attached to this memorandum -- I thought it would be useful to have OSR answer your question on adding up the Soviet military estimates. The objective of OSR's program analysis is to assure that the estimates of Soviet military forces -- missiles, aircraft, ships, tanks, men -- don't make the Soviet soldier look either larger or smaller than he is.

4. Using the 1967 estimate cycle as the example, we started with analysis performed for NIE 11-8-67. Each responsible OSR branch prepared detailed force statements on the production and procurement of major military hardware (missiles, submarines, bombers), on

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the construction of sites or bases, and on the operational deployment of military units for each year under study. Then we put these data on the computer and integrated them with previously prepared operating cost factors and equipment prices.

5. These calculations told us that the Soviet commitment to the strategic attack mission absorbed resources equivalent to \$6.3 billion in 1967. They also told us what the cost of this mission would be during each of the next ten years, if these forces evolve as estimated.

6. The process was repeated as we worked on NIE 11-3 for the Soviet strategic air and missile defense mission, and on NIE 11-14 for the general purpose forces.

7. We are now reexamining the force statements, updating them on the basis of the latest intelligence, and adding in such matters as Soviet expenditures for military research, development, test, evaluations, and space. This will all go on the computer in time to back up the preparation of NIE 11-4 on Soviet military policy.

8. The OSR results are meshed with OER estimates for civilian economic activities to round out the estimate of the USSR's GNP. In this way, we can evaluate the economic feasibility or impact of the estimated military activities.

9. The work of OSR in effect re-creates the Soviet military budget in detail comparable to the Five Year Defense Program and the budget submission of the Secretary of Defense. This is how we bring all the estimates up together and examine their impact on the Soviet economy.

/s/

R. J. SMITH
Deputy Director for Intelligence

Attachment: a/s

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Rubles, Dollars, and Military Spending

1. We build up our estimates of Soviet defense spending piece by piece, much as military budgets are prepared in this country.

a. For many years, using all sources of information, we have recorded and cataloged the major elements that make up Soviet military forces -- divisions, aircraft, ICBMs, ships and so on.

b. We have established the quantities of men, other equipment and material associated with each of these elements.

c. This detailed information is kept in the memory of a large computer for the past, the present, and as projected for the future -- almost three decades in all.

d. As newer information becomes available, the information in the computer is updated and refined.

2. To calculate the cost of the various programs, we apply ruble prices as well as dollar prices to all of the quantities, add up the results, and get figures for total defense spending in both rubles and dollars.

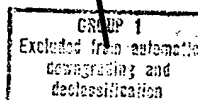
a. Separate ruble and dollar calculations are necessary because

1) the official exchange rate is unrealistic and

2) the relative cost of goods and labor in Communist economies and free economies are inherently different.

3. The ruble figures show how the costs of the military programs or missions look in Soviet terms and how various programs compare with each other.

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a. They provide a Soviet view of defense spending as a whole and how it eats into spending for industrial or agricultural investment or consumer welfare.

4. The equivalent dollar figures enable US planners to understand the size of Soviet defense programs and activities in terms that allow direct comparisons with US programs.

5. Example: Soviet military personnel costs

a. We estimate Soviet military personnel costs at an average of 1400 rubles per man per year. When we price these in equivalent dollars, the figure is \$5300 -- a ratio of about \$4 to each ruble.

b. If we were to convert the 1400 ruble figure at the official rate of exchange -- \$1.11 to the ruble -- the result would make it appear that the average cost of Soviet military personnel, in US terms, was equivalent to about \$1540 per man, instead of \$5300. This would be entirely unrealistic.

c. Equipment costs show similar relationships. For example, we estimate that a large air defense radar costs the Soviets about 600,000 rubles. To build this same radar in the US would cost about one million dollars. The ratio in this example is about \$1.65 to the ruble, quite different from that of military pay and allowances. Even in the case of military equipment the relationship is still different from the official exchange rate.

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